



BANK OF CANADA
BANQUE DU CANADA

Business Outlook Survey

Conducted by the Bank's Regional Offices

Results of the Summer 2008 Survey

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Overview

- Despite the recent slowdown in real economic growth in Canada, the results of the summer survey do not suggest widespread weakness across Canadian firms. Firms have, however, become increasingly concerned about pressures on input costs and inflation.
- The balance of opinion regarding future sales growth edged up, but remains near zero, suggesting a pace of sales growth similar to that over the past 12 months. The balance of opinion on investment rose sharply, and hiring intentions remain solid. Nonetheless, regional differences remain pronounced.
- Capacity pressures are little changed from their level in the spring survey, yet the balances of opinion on input and output prices rose to new highs and inflation expectations increased sharply, owing largely to the persistent strength in the prices of energy and other commodities.

Business Activity

On balance, firms reported an increase in sales growth over the past year; however, the balance of opinion on past sales activity edged down and remains well below 2007 levels (**Chart 1**). The balance of opinion on future sales growth moved back into positive territory but remains close to zero, suggesting little change in the pace of sales growth over the next 12 months (**Chart 2**). On balance, firms located in Western Canada are expecting an increase

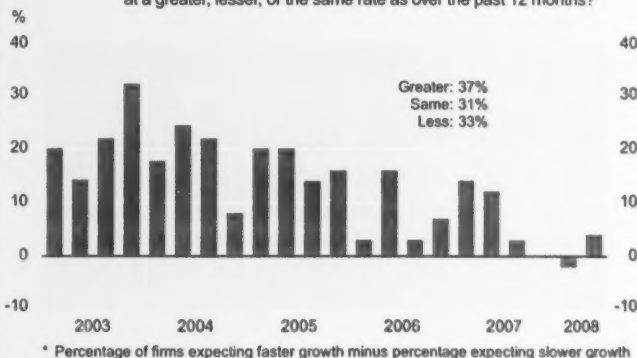
Chart 1 Past Sales Growth: Balance of Opinion*

Over the past 12 months, did your firm's sales volume increase at a greater, lesser, or the same rate as over the previous 12 months?



Chart 2 Future Sales Growth: Balance of Opinion*

Over the next 12 months, is your firm's sales volume expected to increase at a greater, lesser, or the same rate as over the past 12 months?



The Business Outlook Survey summarizes interviews conducted by the Bank's regional offices with the senior management of about 100 firms selected in accordance with the composition of Canada's gross domestic product. The survey's purpose is to gather the perspectives of these businesses on topics of interest to the Bank of Canada (such as demand and capacity pressures) and their forward-looking views on economic activity. Additional information on the survey and its content is available on the Bank of Canada's website at <www.bankofcanada.ca/en/bos/index.html>. The summer survey was conducted from 20 May to 13 June 2008.

The opinions expressed are those of the respondents and do not necessarily reflect the views or policies of the Bank of Canada. The method of sample selection ensures a good cross-section of opinion. Nevertheless, the statistical reliability of the survey is limited, given the small sample size.

in sales growth over the next year, while those based in Central and Eastern Canada are expecting sales growth to slow. Overall, strong commodity prices and expectations of still-healthy domestic demand are helping to offset the negative effects of a weak U.S. economy and a strong Canadian dollar on the sales outlook.

The balance of opinion on investment in machinery and equipment moved back up sharply in this survey (Chart 3). This increase was driven by firms based in Central and Eastern Canada, with many planning higher investment spending for reasons related to restructuring. Intentions to increase investment remain strongest in Western Canada, where firms are looking to alleviate capacity pressures.

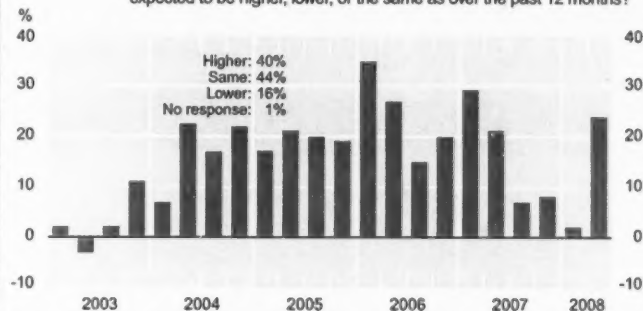
The balance of opinion on employment is unchanged from its level in the spring survey and remains solidly positive (Chart 4). Nonetheless, firms in the manufacturing sector, or located in Central and Eastern Canada, were less likely to expect to increase employment than other firms.

Pressures on Production Capacity

The percentage of firms reporting that they would have difficulty meeting an unexpected increase in demand edged up from its level in the spring survey (Chart 5). Nonetheless, reports of capacity pressures remain below the elevated levels recorded in 2007, and the percentage of firms reporting significant difficulty has eased from recent highs. Capacity pressures continue to be more pronounced among firms located in Western Canada, particularly those in the Prairies.

Chart 3 Investment in Machinery and Equipment: Balance of Opinion*

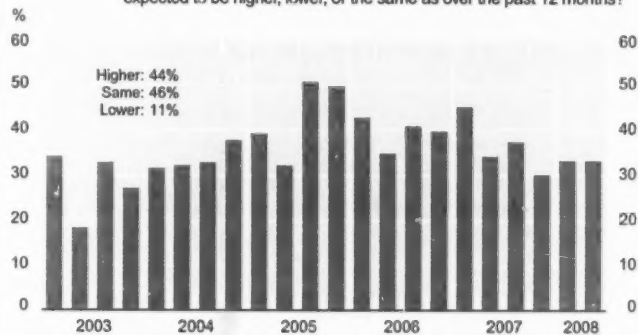
Over the next 12 months, is your firm's investment spending on M&E expected to be higher, lower, or the same as over the past 12 months?



* Percentage of firms expecting greater investment minus the percentage expecting less investment

Chart 4 Future Employment Level: Balance of Opinion*

Over the next 12 months, is your firm's level of employment expected to be higher, lower, or the same as over the past 12 months?



* Percentage of firms expecting higher levels of employment minus the percentage expecting lower levels

Chart 5 Ability to Meet Demand

How would you rate the current ability of your firm to meet an unexpected increase in demand?

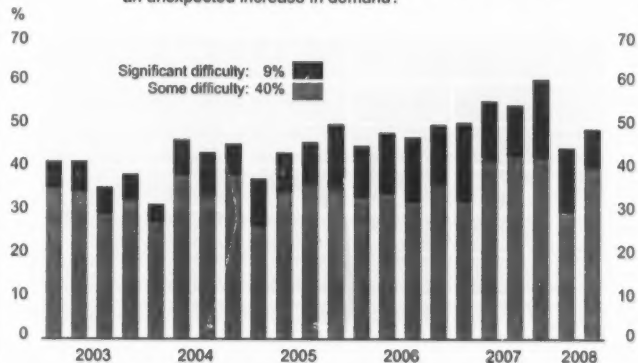
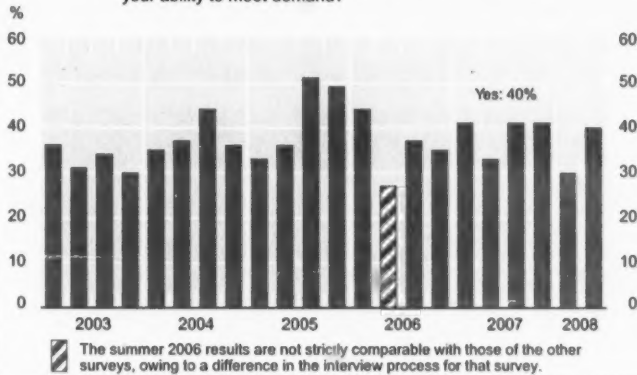


Chart 6 Labour Shortages

Does your firm face any shortages of labour that restrict your ability to meet demand?



The percentage of firms reporting that labour shortages are restricting their ability to meet demand moved back up to its level in the autumn and winter surveys (**Chart 6**). Labour shortages continue to be more prevalent in Western Canada, particularly in British Columbia.

Chart 7 Input Price Inflation: Balance of Opinion*

Over the next 12 months, are prices of products/services purchased expected to increase at a greater, lesser, or the same rate as over the past year?



Prices and Inflation

The balances of opinion for both input and output prices are at record-high levels for the survey. The expected increase in input price growth over the next 12 months (**Chart 7**) stems largely from the continuing strength in the prices of oil and other energy commodities, in combination with the higher prices of food and other non-energy commodities such as base metals. Some firms also cited rising prices of imports from China. The balance of opinion on input prices is positive for all sectors and all regions.

Chart 8 Output Price Inflation: Balance of Opinion*

Over the next 12 months, are prices of products/services sold expected to increase at a greater, lesser, or the same rate as over the past year?

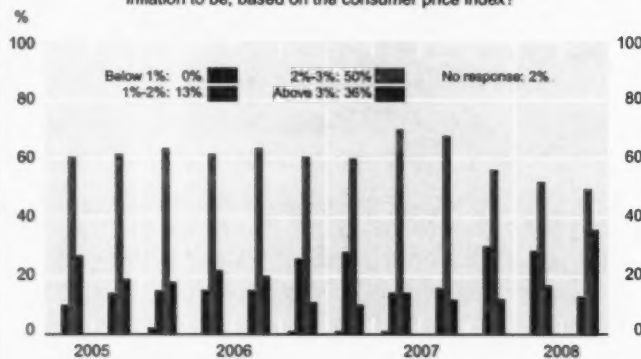


On balance, firms also expect their own output prices to increase at a greater rate over the next 12 months (**Chart 8**). Many firms plan to at least partially pass their higher costs through to their output prices, and they expect their competitors to do the same. The balance of opinion on output prices remains lower than that for input prices, however, since some firms still feel unable to pass through higher costs because of competitive pressures.

Firms' expectations about total CPI inflation have also moved up sharply, owing mainly to higher energy prices (**Chart 9**). The percentage of firms expecting inflation to be above 3 per cent over the next two years has increased to 36 per cent—higher than in any previous survey—while the percentage expecting inflation to be within the Bank's target range of 1 to 3 per cent has fallen from 80 per cent in the spring survey to 63 per cent in this survey.

Chart 9 Inflation Expectations

Over the next two years, what do you expect the annual rate of inflation to be, based on the consumer price index?

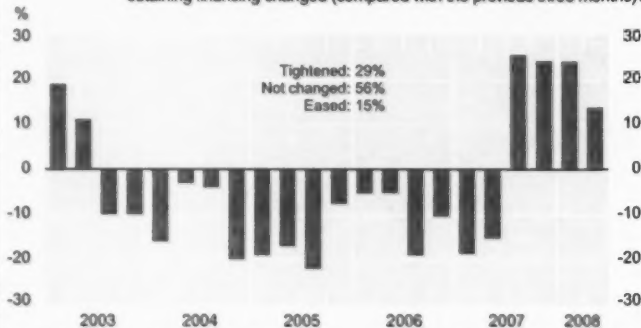


Credit Conditions

The balance of opinion on credit conditions remains positive, indicating that the terms and conditions for obtaining financing tightened over the past three months (**Chart 10**). However, fewer firms reported a tightening in credit conditions than in the previous survey.

Chart 10 Credit Conditions: Balance of Opinion*

Over the past three months, how have the terms and conditions for obtaining financing changed (compared with the previous three months)?



* Percentage of firms reporting tightened minus percentage reporting eased. For this question, the balance of opinion excludes firms that responded "not applicable."

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